

THE BIG \$PLIT

INCOME SPLITTING'S UNEQUAL
DISTRIBUTION OF BENEFITS
ACROSS CANADA



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EXECUTIVE SUMMARY

A study by Tristat Resources commissioned by the Broadbent Institute finds that the majority of Canadian families with children under 18 would get no benefit at all from the Conservatives' income splitting scheme, despite this group being the express target of the tax policy. Fewer than 4% of families with children under 18 are eligible for a benefit in excess of \$5,000, while two out of three of the targeted families would receive less than \$500.

Conducted by statistician Richard Shillington, the study uses Statistics Canada's Social Policy Simulation Database/Model (SPSD/M)¹. It adds to existing literature by taking a detailed look at which types of families stand to benefit in terms of the combination of earnings and tax brackets. It also shows the significant variation in distribution in benefits that would be felt across the provinces if the policy were adopted.

“The majority of Canadian families with children under 18 would get no benefit at all from the Conservatives' income splitting scheme, despite this group being the express target of the tax policy.”

The proportion of families with children under 18 getting no benefit is highest in Quebec (61.1%), Prince Edward Island (57.6%), Manitoba (55.7%) and New Brunswick (55.0%). It is lowest in Alberta (44.1%). In addition, the average benefit² – which disguises the fact that the majority of families with children under 18 get nothing – varies significantly by province too. It is highest in Alberta at \$1,359, and lowest on Prince Edward Island (\$488) and Quebec (\$510).

The benefits skew heavily toward traditional families with one high-income breadwinner.

Across Canada, only 13.8% of families with children under 18 would gain a benefit from family income splitting of \$2,000 or more. This is true of just 7.4% of such families in Quebec, 8.1% in P.E.I, and 12.1% in New Brunswick. By contrast, 22.8% of Alberta families with children under 18 would gain \$2,000 or more. Thus even for the small minority of families that will see such a benefit, there are meaningful provincial differences.

“Nine out of 10 Canadian households would receive no benefit at all from the proposed tax policy. Under 1% of all households would be eligible for benefits in excess of \$5,000.”

In line with other studies that show the Conservatives' income-splitting policy overwhelmingly favours certain high-income traditional families, this report finds that nine out of 10 Canadian households (families with and without children and those living alone) would receive no benefit at all from the proposed tax policy. Under 1% of all households would be eligible for a benefit in excess of \$5,000.

OTHER KEY FINDINGS:

- The average benefit of income splitting across all households is only \$185, though nine out of 10 households will receive nothing. When one factors in the \$3 billion cost in lost federal revenues that will result from this tax policy, income splitting stands to impose net costs on many Canadian households.
- To gain from income splitting, a family with children under 18 must have two parents in different tax brackets to share income. Thus single parent families (20.2%) and those with partners in the same tax bracket (28.9%) are automatically excluded from benefitting. The detailed calculations accounting for available refundable and non-refundable tax credits estimate that 54.1% of families would see no benefit.
- Just 1.7% of all Canadian families with children under age 18 – those who have one earner in the top tax bracket of 29% and another parent who pays a zero tax rate – would be eligible for the maximum benefit.
- The biggest winners from income splitting would come from the 3.7% of families with a single spouse breadwinner able to shift \$50,000 of taxable income from the top tax bracket to the bottom rates of zero and 15%, resulting in an average benefit of more than \$7,000.

In summary, this report provides insight into who wins and who loses in the Conservatives' proposed income splitting policy. It puts forth clear evidence that the majority of families with children under 18, as well as nine out of 10 households, will see no benefit at all from the tax measure.

Where significant benefits do accrue, they are to higher-income families, particularly those in a traditional model. This policy, which benefits a higher proportion of families in some provinces than others, stands to increase income inequality in Canada.

BACKGROUND

The purpose of this report is to determine how many and which type of families will or will not benefit from the income splitting proposal advocated by the Conservatives. The report offers a detailed look at who benefits based on the combination of earnings and tax brackets for different families as well as what the regional variation in benefits looks like.

The Conservatives' proposal would allow families with children under 18 to shift up to \$50,000 of taxable income from the higher-income spouse to their lower-income partner. This proposal has already been studied by the C.D. Howe Institute in 2011³, and more recently by the Canadian Centre for Policy Alternatives (CCPA)⁴. These studies have estimated the proposals' cost to the federal treasury at \$2.7 billion for 2012 and \$3 billion for 2015. This report examines only federal tax changes; there will be additional losses to provincial treasuries if provinces were to follow suit and implement income splitting too.

Before considering the research findings, certain features of the income splitting proposal should be highlighted:

- The value of income splitting depends on the amount of taxable income shifted and the difference between the higher and lower marginal tax rates.
- Some families will get no benefit because they are single parents. Other parents will get no benefit because they are in the same tax bracket.
- The exact benefit depends not only on tax brackets. There would be negligible benefits for families with one earner in the lowest tax bracket and a partner with no earnings since shifting income would lead to the loss of the spousal credit. Available tax credits could also influence the exact benefit.
- Some parents will only get a small benefit because their tax brackets are very similar.

- The maximum spread in marginal tax rates will happen in families where the higher income spouse is in the highest tax bracket (taxable incomes in excess of \$136,270) and the lower-income spouse has no income. The federal income tax brackets can be referenced in Table 1.
- In order to take full advantage of income splitting (shifting \$50,000 to a spouse), the higher-income spouse will need a taxable income that is at least \$100,000 more than that of the lower-income spouse.

TABLE 1 - FEDERAL INCOME TAX BRACKETS ASSOCIATED WITH MARGINAL TAX RATES, 2014

THE INCOME ASSOCIATED WITH VARIOUS TAX BRACKETS, 2014	
Marginal Tax Rates	Taxable Income
0%	Less than \$11,038
15%	\$11,038 - \$43,953
22%	\$43,953 - \$87,907
26%	\$87,907 - \$136,270
29%	\$136,270 and over

This report estimates the proportion of families in various combinations of tax brackets, then estimates the proportion receiving different levels of benefit and the provincial variation in these figures.⁵

METHODOLOGY

The data source for these tabulations is Statistics Canada's Social Policy Simulation Database/Model (SPSD/M). CCPA shared their version of the model for the calculations presented here. This model provides estimates for the year 2015, based on the income of Canadians and their tax brackets, of the impact of the proposed income splitting policy. These data, including information on the presence of children, are available by province.

These data were used to provide the results presented in the tables and charts below.⁶ The analyses here show both the number of families with children under 18 and households (families with and without children and those living alone) who would benefit from income splitting and by how much.

RESULTS

The results presented in Table 2 depict which types of families with children under age 18 (those families the Conservative policy targets) stand to benefit from income splitting based on combinations of earnings from different income brackets. These values represent the proportion of families with different tax bracket combinations. (Those partners in the lowest tax bracket who paid no income tax are shown as "no taxes".)

TABLE 2 - PROPORTION OF FAMILIES WITH CHILDREN UNDER 18 BY THE TAX BRACKET COMBINATIONS OF PARTNERS, 2015

		LOWER TAX BRACKET PARTNER						Total
		No partner	No taxes	15%	22%	26%	29%	
HIGHER TAX BRACKET PARTNER	No taxes	10.6%	9.8%	0.0%	0.0%	0.0%	0.0%	20.4%
	15%	3.7%	7.0%	9.8%	0.0%	0.0%	0.0%	20.5%
	22%	4.8%	10.0%	16.6%	8.3%	0.0%	0.0%	39.8%
	26%	0.6%	3.4%	4.0%	4.3%	0.7%	0.0%	13.0%
	29%	0.4%	1.7%	1.4%	1.5%	1.0%	0.3%	6.2%
	Total	20.2%	31.9%	31.8%	14.2%	1.7%	0.3%	100%

We see using the shaded cells that 28.9% of families are in the same tax bracket and 20.2% are single parents. Combined then, about half of families are in tax brackets where they are ineligible to get any benefit from income splitting. (The detailed calculations accounting for available refundable and non-refundable tax credits, outlined below, estimate that 54.1% of families would see no benefit.)

Many families with two earners in adjacent tax brackets will gain comparatively little since the two brackets are very close (eg 22% and 26%; 26% and 29%), and/or because the higher earner has only modest taxable income above the threshold of the higher tax rate that can be shifted to the lower rate.

Only 1.7% of families have a higher-income spouse in the top tax bracket and the lower-income spouse paying no tax. Nevertheless, it is this type of family that is eligible to get the maximum benefit from the tax policy.

WHICH FAMILIES WIN AND LOSE?

The actual benefit from income splitting depends not only on the tax bracket combinations of two partners but also available refundable and non-refundable tax credits. Below, Table 3 presents data on the number of families with children under 18 by their estimated tax reduction from income splitting.

TABLE 3 - NUMBER OF FAMILIES WITH CHILDREN UNDER 18, BY VALUE OF INCOME-SPLITTING, 2015

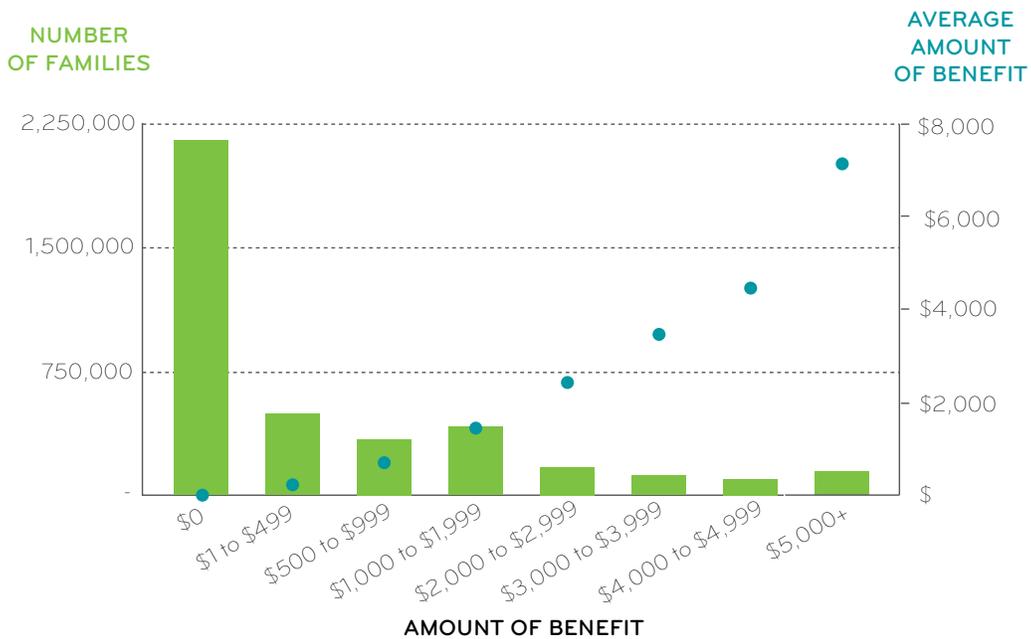
BENEFIT RANGE	PERCENT	NUMBER OF FAMILIES	AVERAGE BENEFIT (\$)
Zero	54.1%	2,135,000	\$ –
\$1-499	12.8%	505,000	\$254
\$500- \$999	8.8%	346,000	\$725
\$1,000-\$1,999	10.6%	419,000	\$1,441
\$2,000-\$2,999	4.5%	176,000	\$2,434
\$3,000-\$3,999	3.1%	122,000	\$3,490
\$4,000-\$4,999	2.5%	98,000	\$4,462
\$5,000 +	3.7%	147,000	\$7,128
Total	100.0%	3,949,000	\$841

The data show clearly how few Canadian families will see significant benefits from income splitting. Overall, 54.1% of families with children under 18 will get no benefit,⁷ while another 12.8% of these families will receive less than \$500 in benefit. That's two out of three targeted families that will receive less than \$500. Fewer than 14% of such families will receive \$2,000 or more, and very few families with children under 18 – 3.7% – will be eligible for a benefit in excess of \$5,000.

Note that averages can be skewed by a very few, very large values. That is what has occurred here. Though the majority of families with children under 18 get no benefit or \$0, the average benefit across the country comes out to \$841. This is due to the unequal distribution of benefits, where the few families with a single spouse breadwinner able to shift \$50,000 of taxable income from the top tax bracket to the bottom rates of zero and 15%, get savings of more than \$7,000, pulling up the average.

A detailed breakdown of the distribution of benefits listed in Table 3 is depicted in Graph 1 below, further demonstrating how unequal the distribution of benefits is.

GRAPH 1: DISTRIBUTION OF FAMILIES WITH CHILDREN UNDER AGE 18 BY THE BENEFIT OF INCOME SPLITTING



WINNERS AND LOSERS: WHICH FAMILIES GAIN BY PROVINCE

Below, Table 4 depicts the distribution of benefits from income splitting within each province, allowing for an analysis of variation between them.

TABLE 4 - PROPORTION OF BENEFIT AND AVERAGE BENEFIT FOR FAMILIES WITH CHILDREN UNDER 18, 2015

	NO BENEFIT	UNDER \$2,000	\$2,000 - \$5,000	OVER \$5,000	AVERAGE BENEFIT*
Quebec	61.1%	31.4%	6.1%	1.3%	\$510
Prince Edward Island	57.6%	34.3%	7.2%	0.9%	\$488
Manitoba	55.7%	29.5%	12.2%	2.6%	\$772
New Brunswick	55.0%	32.9%	8.2%	3.9%	\$787
British Columbia	53.8%	31.8%	10.1%	4.2%	\$853
Ontario	53.3%	32.5%	10.7%	3.4%	\$874
Saskatchewan	52.3%	28.2%	13.3%	6.2%	\$1,070
Nova Scotia	52.2%	34.5%	11.6%	1.7%	\$727
Newfoundland & Labrador	46.7%	38.1%	10.9%	4.3%	\$925
Alberta	44.1%	33.1%	13.8%	9.0%	\$1,359
All Provinces	54.1%	32.2%	10.0%	3.7%	\$841

*Average over all families including those with no benefit.

The results indicate that the proportion of families with children under 18 getting no benefit is highest in Quebec (61.1%), Prince Edward Island (57.6%), Manitoba (55.7%) and New Brunswick (55.0%). That is compared to 54.1% for Canada as a whole. The figure is lowest, though still high, in Alberta, where 44.1% of such families will be left out of getting any benefits.

The proportion of families with children under 18 where benefits would be \$2,000 or more is highest in Alberta at 22.8% and lowest in Prince Edward Island at 8.1% and Quebec at 7.4%.

“When one considers that all Canadians will be affected by the \$3 billion loss in federal tax revenue needed to pay for income splitting, the value of the benefit becomes particularly low.”

The average benefit of income splitting for families with children under 18 also shows stark variation. Highest in Alberta at \$1,359, it is lowest in Prince Edward Island at \$488 and in Quebec at \$510. Again, these averages disguise the fact that the majority of families with children under 18 across the country (54.1%) will get nothing, and that two out of three of these families will get less than \$500.

There are three groups that cannot benefit from income splitting: families without children, families with children 18 or older, and unattached individuals (those who live alone). If these household types are included in the analyses (see Table 5), then 89.9% of all Canadian households stand to gain no benefit from income splitting.

The average benefit of income splitting, when all households are considered, is a mere \$185 across the country. It would be highest in Alberta at \$332 and lowest in Quebec at \$106. Nine out of 10 households, again, would get nothing.

When one considers that all Canadians will be affected by the \$3 billion loss in federal tax revenue needed to pay for income splitting, the value of the benefit becomes particularly low. The \$3 billion loss in federal revenue, shared across Canada's approximately 35 million people, amounts to a cost of about \$85 per person or \$340 for a family with two parents and two children (a cost

that will be felt either as cuts in government spending or increases in other taxes.) Income splitting would thus come at a net cost to the 54.1% of families with children under 18 and 89.9% of households that stand to get no benefit from the policy. It would also come at a net cost to those additional families that stand to get less than \$85 per person in benefit (or \$340 for a family of four).

TABLE 5- PROPORTION OF BENEFIT AND AVERAGE BENEFIT FOR ALL HOUSEHOLDS*, 2015

	AVERAGE BENEFIT**	NO BENEFIT	UNDER \$2,000	\$2,000 - \$5,000	OVER \$5,000
Quebec	\$106	92.0%	6.5%	1.3%	0.3%
Prince Edward Island	\$113	90.2%	7.9%	1.7%	0.2%
Nova Scotia	\$140	90.8%	6.7%	2.2%	0.3%
New Brunswick	\$167	90.4%	7.0%	1.8%	0.8%
British Columbia	\$174	90.6%	6.5%	2.1%	0.9%
Manitoba	\$185	89.4%	7.1%	2.9%	0.6%
Ontario	\$199	89.4%	7.4%	2.4%	0.8%
Newfoundland & Labrador	\$200	88.5%	8.2%	2.4%	0.9%
Saskatchewan	\$242	89.2%	6.4%	3.0%	1.4%
Alberta	\$332	86.3%	8.1%	3.4%	2.2%
All Provinces	\$185	89.9%	7.1%	2.2%	0.8%

* Includes families with and without children and unattached individuals.

** Average over all families including those with no benefit.

CONCLUSIONS

This report provides much needed insight into the likely impact on families of the Conservatives' proposed income splitting policy. It provides clear evidence that their stated intention of helping Canadian families with children under 18 is not served well by the policy. The results show that income splitting would provide no benefit to a majority of families (54.1%) with children under 18, and nothing to nine out of 10 Canadian households. Where significant benefits do accrue, they are to higher-income families with a traditional family model of one breadwinner and a stay at home spouse. The benefits also skew more towards families in Alberta, and less towards families in Quebec, Prince Edward Island, Manitoba and New Brunswick.

“If the intention is truly to help Canadian families, the Conservative government should scrap its plan to introduce this costly tax scheme – one that stands to increase income inequality.”

The late Jim Flaherty, former Finance Minister, summed income splitting up well when he said it “benefits some parts of the Canadian population a lot. And other parts of the Canadian population virtually not at all.” If the intention is truly to help Canadian families, the Conservative government should scrap its plan to introduce this costly tax scheme – one that stands to increase income inequality.

ENDNOTES

- ¹ The estimates in this report rely on the CCPA's "glass box" version of Statistics Canada's Social Policy Simulation Database and Model (SPSDM) version 21.0. The assumptions and calculations underlying the simulation results were prepared by the author and the responsibility for the use and interpretation of these data is entirely that of the author. The author would like to thank the Canadian Centre for Policy Alternatives and specifically David MacDonald for sharing their version of Statistics Canada's SPSSD/M.
- ² In this report, "average benefit" refers to the mean benefit.
- ³ C.D. Howe Institute; *Income Splitting for Two-Parent Families: Who Gains, Who Doesn't, and at What Cost?*; Laurin A. and Kesselman, J.; October 2011.
- ⁴ Canadian Centre for Policy Alternatives; *Income Splitting in Canada; Inequality by Design*; Macdonald, D. January 2014.
- ⁵ The report does not address the full range of labour market incentive, tax policy principles or equity arguments for or against the proposal.
- ⁶ All results in the report tables show values rounded to one decimal point. When these values are added together, sums may differ very slightly from the actual totals shown.
- ⁷ This estimate differs from the 49.1% combined figure outlined in Table 2, which represents the proportion of families ineligible for benefits based solely on looking at the combination of their respective tax brackets. When available refundable and non-refundable tax credits are factored into estimates of the new tax reduction, some additional families (54.1%) get no benefit from income splitting.